

MOST WHISTLEBLOWER SYSTEMS ARE INCOMPLETE AND COST MORE IN THE LONG RUN



EXECUTIVE SUMMARY

The Sarbanes-Oxley Act ("SOX") requires a system that records complaints regarding accounting matters and internal accounting controls. To comply with this requirement, alternatives include a call center (aka "hotline"), and internal solutions. In most cases, these alternatives:

- Cost more, when one considers the combined cost of collecting, investigating, and resolving complaints, and
- Allow allegations of retaliation, which in turn triggers the severe penalties and employee protections contained in SOX.

Of course, no one purposefully designs a poor system, but the majority of internal solutions and outside vendors provide this result. For example:

- Most internal solutions (when either collecting or investigating complaints) provide an unacceptably high risk of encouraging retaliation claims. Any money saved by using internal resources is immediately lost when the first retaliation claim occurs.
- By relying on a single collection vehicle (phones), "hotline" services provide an incomplete solution that unnecessarily constrains communications.
- By using inflexible and overly simplistic scripts/forms, most outside vendors fail to collect important information.
- By using unskilled personnel to collect the complaints, uninformed or prank calls waste investigation resources, rather than being quickly identified for what they are.

Fulcrum addresses these challenges by using skilled forensic accountants to collect, interpret, and resolve complaints. This eliminates waste caused by having insufficient information from the initial contact. The total cost, measured from when the complaint occurs to when the Audit Committee agrees that the matter is fully resolved, is significantly less.

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Section 301(4) of the Sarbanes-Oxley Act ("SOX") requires procedures for the collection and resolution of employee complaints covering an extremely broad range of financial and accounting control issues. The system must allow for anonymous and confidential submissions.

ARE THESE LAWS SERIOUS?

In a word, **YES!** Compliance with SOX is required as part of U.S. securities laws. Companies not complying will be delisted.

However, the whistleblower provisions also have important employment ramifications. No retaliation of any sort may occur against any employee making a complaint. Interestingly, the employee receives broad protection whenever he "reasonably believes" that a violation may have occurred - the employee need not actually be correct.

SOX provides broader civil and criminal protections than any other whistleblower protection law, such as those involving environmental, harassment, or health/safety offenses. Civil remedies (SOX Section 806) include the right to reinstatement,

Fulcrum has a unique approach that includes a competitive phone solution.

Hotline companies cannot match a forensic accountant's ability to:

- Quickly identify uninformed or prank complaints;
- Gather sufficient information to ensure that investigations and other follow-up are complete and efficient;
- Provide a complete solution, rather than simply turning the problem over to you.



Savings from internal systems are lost when claims of retaliation or lack of independence occur.

back pay with interest, and the cost of pursuing the employee's claim. Criminal provisions (SOX Section 1107) make it a felony to retaliate against a whistleblower, and are punishable by up to ten years in prison and large fines. The criminal penalties apply to both the employer and to individual managers, such as human relations executives, a whistleblower's supervisor, or anyone else who fails to handle a complaint properly.

The Occupational Safety and Health Administration (OSHA) within the U.S. Department of Labor (DOL) investigates SOX cases claiming retaliation. OSHA has already received numerous complaints under SOX. DOL administrative law judges are responsible for related trials, with appeals initially going to the DOL's Administrative Review Board. If the DOL procedure (including appeals) is not completed within 180 days (which rarely occurs), the employee may opt for a new trial in U.S. District Court. Some well-known and reputable companies have already been sued in this manner.

WHY SHOULD A WHISTLEBLOWER SOLUTION BE OUTSOURCED?

To save money, some companies are considering an internally operated system. In the long-term, cost savings from internal solutions are almost impossible to achieve, especially for smaller firms. Unless your company has tens of thousands of employees, your internal solution is likely to have the following shortcomings:

1. Internal resources receiving complaints will eventually be implicated (either directly or indirectly) by a complaint. This does not mean, of course, that the complaint is meritorious. If handling whistleblower complaints internally causes additional allegations of impropriety, any perceived cost savings will quickly disappear. Independence requires outside involvement.

2. Sufficient anonymity may not exist. Modern technology and computer systems allow tracing of most communications within the company. The risk of retaliation claims increases with greater internal involvement.

Failures in either of these areas are costly. The costs of additional investigation, legal fees and retaliation claims far outweigh any savings gained by attempting to handle this area internally. In the long run, involvement by an outside professional is the cost-effective answer.

WHY ARE PHONE HOTLINES AN INCOMPLETE SOLUTION?

The initial receipt of whistleblower complaints is the smallest part of a whistleblower solution, and is only the first step. When complaints come into a hotline company, an operator will usually follow a set script and obtain basic information. This information is submitted to the client, who must investigate and ultimately resolve the complaint. With only incomplete information (because appropriate follow-up questions were not part of the script), the company must decide:

1. Is the complaint serious?
2. How widespread could this problem be?
3. Who should investigate?
4. How should the investigation be managed in order to maintain anonymity and prevent retaliation?

A trained accountant should be the first involved with any audit or accounting issue. Telephone operators using a script cannot be expected to:



"Hotline" companies aggravate problems with meritless complaints.



Written comments are often more thoughtful, and easier to address. Don't rely solely upon phone contact.

1. Understand the terminology and complexities involved with accounting, auditing, and internal accounting controls;
2. Ask follow-up questions that will facilitate a further investigation and ultimate disposition;
3. Implement any policy guidelines established by your Audit Committee.

We recommend accepting complaints using all standard forms of business communication. This (i) improves the possibility that important documents will be received, (ii) improves the anonymity of complaints that wish to be submitted in this fashion, and (iii) makes the process more available and convenient. Unlike phone hotline companies, we accept complaints via phone, fax, email, web-based form, or snail mail. In our experience, the most thoughtful and helpful information comes in writing, and not from phones.

CAN FULCRUM HELP WITH MERITLESS COMPLAINTS?

Unfortunately, any SOX-compliant whistleblower system will gather meritless complaints. Unlike other approaches, Fulcrum can help limit the resources spent in this area.

Complaints received under SOX are dramatically different from the safety and sexual harassment claims where hotline companies gained experience. Complaints generated by SOX's whistleblower provisions are likely to be one of the following:

1. A nuisance or prank call may come from a poorly performing employee who thinks that a whistleblower complaint will protect his job, or from someone simply trying to cause trouble. A trained accountant can identify these by asking focused follow-up questions that are specific to the allegation. When a hotline company is employed, company resources are needlessly involved in these trivial complaints. The hotline company escalates the complaint from minor to seemingly serious.

2. A well-meaning but ill-informed employee may not understand complex accounting requirements. A trained accountant can properly educate such a person as to why their concern is actually not a problem. In contrast, a hotline employee following a script will accentuate the complaint. This wastes resources to research an incomplete report that was never really a problem.
3. Some complaints can be handled appropriately by your existing internal procedures. Examples include inappropriate expense reimbursements, and employee inventory thefts. Complaints involving non-financial violations of company policy, such as sexual harassment issues and protests of performance reviews, may also be reported. When this occurs, we gather information professionally, and promptly turn the matter to the department or group that you designate.
4. Serious claims of financial fraud will be infrequent, but require expertise. These contacts must be thoroughly understood, reported to the proper persons within your organization, and investigated by those that are truly independent.

WHAT DOES FULCRUM'S SOLUTION COST?

Fulcrum currently has three pricing plans. Select the one that is best for you.

1. We charge only for the time spent fielding and resolving complaints, billed at our normal hourly rates. Our rates average around \$200 per hour.
2. We will match your lowest bid from any reliable hotline company. For this matched price, we handle all calls of 10 minutes or less at no additional cost. Any call exceeding 10 minutes occurs because we are gathering information and resolving concerns in a manner that the hotline companies

	Fulcrum Financial Inquiry	Hotline Companies	Internal Solution
Will log and report all calls.	X	X	X
Expert in accounting and internal controls	X		Depends on who is involved
Maintains required anonymity throughout a complete solution	X		
Has the expertise to help establish policies	X		X
Will use a broad variety of communication tools (fax, web-based, email, snail mail, etc.) that you specify	X		X But, may violate required anonymity
Can receive calls in multiple languages	X	X	

are incapable of doing. Therefore, we bill for the portion of a call that exceeds 10 minutes at our normal hourly rates.

3. We charge \$6 per employee, with **no minimums**. This option is for smaller companies where minimum charges cause the per employee amount to be higher. For this price, we handle all calls of 10 minutes or less at no additional cost. Any call exceeding 10 minutes occurs because we are gathering information and resolving concerns in a manner that the hotline companies are incapable of doing. Therefore, we bill for the portion of a call that exceeds 10 minutes at our normal hourly rates.

You can cancel our service at any time, at no additional cost.

THE FULCRUM ADVANTAGE

Fulcrum Financial Inquiry is a forensic accounting firm with significant experience in handling financial investigations, accounting processes, and related dispute resolution. The principal that leads this practice has well over 25 years performing financial investigations and audits. Most of our professionals come from international accounting firms. Our professionals have served numerous public companies. For more information about us, please visit our web site.

Fulcrum provides the following advantages:

1. Our personnel understand the complexities involving the full scope of "accounting, internal control, and auditing matters" required by Sarbanes-Oxley. This allows us to:
 - Gather necessary information immediately, including important follow-up facts,
 - Handle the audit committee directives from beginning to end, and
 - Not waste resources on complaints that involve less serious matters.
2. By being completely independent of your existing workforce and outside auditors, we provide assurance that complaints receive the full and fresh attention they deserve.
3. By operating outside of your company's offices, and being otherwise unaffiliated with your company, we reduce costly assertions that retaliation occurred against someone who lodges a complaint. Preventing a single retaliation claim will more than pay for our entire service.

When serious accounting complaints occur, Fulcrum is available to perform the required additional work. Our capabilities include preserving computerized and paper evidence, performing investigations, and recommending improvements in the accounting systems and internal controls. Having a forensic accounting firm involved from the start provides seamless and rapid service that is otherwise not possible.



Fulcrum's skilled personnel and customized communications cost no more than the hotline cookie-cutter proposals.

WHAT STEPS SHOULD WE TAKE?

Under Section 301(4), a whistleblower system must be in place by your first annual shareholders' meeting held after January 14, 2004, but not later than October 31, 2004. However, Sections 806 and 1107 are already in effect.

We are pleased to customize solutions that are appropriate for your situation. We find that many companies benefit from solutions that include electronic communications, mail, fax and phone. We will alter each of these to meet your needs.

If you need assistance designing the proper procedures to implement, we have the expertise to provide this consulting service. Please call us to discuss your needs.

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No client engagement or other responsibility exists to recipients of this article. You should consult with your own legal and financial advisors to apply the general guidance herein to your specific situation.

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